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OPIC FOR CYNTHIA HOESTLER, JIM HANSLEY

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SUBJECT: JORDAN: POST VIEWS ON ENLARGING INTERARAB FUND

Classified By: Classified by Ambassador Edward W. Gnehm. Reasons 1.5 (b) and (d).

11. (sbu) Summary. In response to proposals to increase the size and nature of OPIC's support for the Amman-based InterArab Fund, Embassy staff took a hard look at the Fund's current activities as well as the factual basis of persistent local rumors about improprieties involving the Fund's management. We found nothing to substantiate these allegations and indeed found evidence to disprove most of them, but we conclude that the InterArab Fund suffers from inadequate management and oversight that has prevented it from making a significant contribution to increasing foreign investment in Jordan. We believe that these deficiencies can be addressed by reorganizing and professionalizing the management of the Fund, putting an enlarged InterArab Fund in a better position to make a significant contribution to Jordan's economic development and U.S. interests here. End Summary.

12. (sbu) In light of Washington's consideration of the possibility of increasing the size and scope of OPIC's support for the InterArab Fund, post is providing the following background on the local activities and reputation of the Fund. The Amman-based Fund is an OPIC-supported investment fund that has a mandate to invest in Jordan, Oman, and the Palestinian territories. Its current authorized size is \$45 million, two-thirds of which can be borrowed from OPIC, with one-third from private investors. We understand that OPIC staff is considering a proposal that would increase the maximum size of the fund to \$105 million and allow the fund to invest all of its assets in Jordan.

FDI in Jordan Low Despite Reforms

13. (c) The success of the InterArab Fund in catalyzing private foreign direct investment in Jordan would be an important complement to the growing bilateral economic relationship between the United States and Jordan. The success of the economic relationship undergirds the United States' unique political and security relationship with Jordan. It reinforces moderate policies and strengthens the hand of King Abdullah and his government in dealing with the homegrown extremism that has its roots in persistent underemployment and poverty. In the region, Jordan's economic success serves as a model to show how open, pro-growth economic policies can foster economic development, poverty alleviation and political stability.

14. (sbu) Over the past decade, Jordan has made impressive strides in opening its economy to foreign trade and investment while maintaining sound macroeconomic policies. Its list of economic reforms and initiatives is impressive, including accession to the WTO, negotiation of a free trade area with the United States, a partnership agreement with the European Union, and bilateral investment treaties with the United States and European countries. In addition, considerable progress has been made in modernizing and deregulating domestic financial and goods markets. The U.S. Government has supported nearly all of these initiatives through technical assistance and policy-conditioned cash grants provided through USAID.

15. (sbu) Jordan's investment performance has been disappointing despite these reforms and a recent surge in export-led GDP growth. A recent country survey by the Atlas Investment Group concluded, "In recent years, gross fixed investment, measured as a percent of GDP, has remained relatively flat and insufficient, averaging around 25% of GDP in the period 1997-2000. Moreover, investments have typically been channeled into non-productive sectors such as construction." While this observation applies to both domestic investment and FDI, foreign investment has been particularly disappointing. With the exception of large inflows associated with the privatization of the telephone and cement companies, there has been little foreign investment in Jordan's manufacturing and nascent high-tech sectors, despite a dynamic young entrepreneurial sector, a relatively skilled and available local workforce and the successful example of the QIZ initiative. (The largest U.S. investment, a joint venture between the Abemarle Co. of

Richmond and the Arab Potash Company is in the mining sector.)

Disappointing Contribution So Far

¶16. (sbu) In this light, the performance of the InterArab Fund in attracting new foreign investment to Jordan has been less than impressive. In four years, the Fund has invested in four projects in Jordan for a total of approximately \$12.7 million. None of these investments currently appears to be generating a return for the Fund or for the Jordanian economy. According to InterArab Fund manager Dr. Fuad Abu Zayyad, the limited use of available funds is explained by existing geographical restrictions on fund investments (only one third of the \$45 million could be invested in Jordan under the current structure).

¶17. (sbu) At the same time, Abu Zayyad says that the narrow range of the Fund's investments is explained by a limited supply of investment grade projects in Jordan. While this is a common complaint of local banks and investors, it appears from embassy's soundings that the InterArab Fund is not well-known in the local business and financial communities as a potential source of financing. Bankers, including those favorable to the fund, describe the fund as inactive, and as not being a partner in the financial community. Thus, the Fund does not appear to be a port of call for investors seeking financing for viable projects. Abu Zayyad acknowledges this, and says the Fund needs to become more active in the community, although he says he has faced resistance as an outsider on the local scene.

Allegations of Improprieties Not Substantiated

¶18. (sbu) There are also persistent rumors of improper activities and business practices associated with the InterArab Fund management. Sources of these rumors include bankers and investors as well as past and present senior government officials. The most significant allegations are,

- 1) That companies in which the fund has invested have paid inflated amounts for land and equipment to parties who are related to fund management.
- 2) That companies in which the fund has invested have sold equipment to parties related to fund management at prices below their value and that the companies themselves are not functioning businesses.
- 3) That fund management is receiving management fees out of line with the fund agreement.
- 4) That there is circular investment among companies in which the fund has invested and the fund itself. That is, that fund management has agreed with companies in which it plans to invest that if those companies invest in the fund (generating contributions from OPIC), the fund will invest in companies at more than their actual value.

¶19. (sbu) Post has worked to carefully assess these allegations and has discussed them extensively with both independent parties and with Dr. Abu Zayyad. We have not been able to find any evidence to substantiate these claims. For example, an allegation that the Jordan Valley Fisheries Company (in which the fund has invested \$4.8 million) paid an excessive amount for the land on which it is located appears to be untrue. The Fund was able to produce documents showing that the fishery leases its land from the Jordan Valley Authority at a nominal rate.

¶10. (sbu) Similarly, we were not able to substantiate the allegation that fund companies have sold equipment and are not actually operational. Post officers visited three of the fund's Jordanian investments (the fishery and the two internet-based ventures) and found each of them to be ongoing enterprises with impressive management, existing sales and business, and prospects for additional business. We were not able to visit the Modern Agricultural Investment Company, located south of the Dead Sea, in which the fund has invested 1.1 million (8% of its assets). Abu Zayyad admits that this is the least promising of the four investments in Jordan and that the company has had difficulty finding competent management. Nevertheless, Abu Zayyad says the MAIC's original Israel-sourced greenhouses are still being used and that the company is under new management and will hopefully turn the corner in 2003.

¶11. (sbu) It was not evident from a brief examination of the fund's financial statements Fund management is receiving fees in excess of those provided for in the fund agreement. In fact, it appears that the InterArab management company has reinvested a substantial portion of the fees it has received back into the Fund.

¶12. (sbu) The suggestion of circular investment appears to be the most serious allegation, and the one that is most difficult for post to assess. Dr. Abu Zayyad asserts that it is the Fund's clear policy not to engage in this practice. In support of this, he showed Econ/C a list of current fund investors. None of those listed were companies in which the fund had an investment interest. However, the 2001 financial statement of Aregon (one of the internet investments) contained a note stating that Aregon had invested in the InterArab Fund. Abu Zayyad and Aregon's general manager said that this was an error. However, both acknowledged that some stockholders in Aregon were also investors in the Corex group, an investor in the InterArab Fund. Since the embassy was not given copies of these documents, we recommend that OPIC look into this issue to its satisfaction, if it has not already done so.

Conclusion: Management Needs Strengthening

¶13. (sbu) The very allegations of improprieties -- combined with the facts that the fund is not well-known or respected in the local business and financial communities and that the fund's investments have yet to generate a return -- suggests that something has not been working. To some extent the fund's poor local image seems to be a function of the fact that nearly all of the investors in the fund are associated with Dr. Abu Zayyad either through family or previous business relationships. In Jordan's factional, family-centered business community, this no doubt contributes to some of the sniping. But in embassy's view, the most fundamental basis of the Fund's problems is inadequate management and oversight. Dr. Abu Zayyad is basically a "one man show," as he admits, and has been seriously ill for much of the last year. He is not supported by an experienced staff and does not seem to have business experience in Jordan.

¶14. (sbu) Post understands that an OPIC consultant who visited Amman in October 2002 prepared a report suggesting a number of ways to improve fund management and oversight. These include hiring professional senior management staff and creating stronger internal controls by strengthening the Fund's investment and advisory committees (expanding the latter to include prominent Jordanians unconnected to the Fund or to Abu Zayyad). We believe that implementing the changes called for in this report will go a long way toward improving the management and the local image of the fund. In addition, a higher profile, strengthened management and broader fundraising should encourage a broader base of investment in the fund. Finally, while allegations of improprieties have not been substantiated, OPIC officials should continue to actively examine and supervise the Fund's activities and investments.

¶15. (sbu) Once the proposed organizational and oversight changes have been implemented, and strengthened professional management is in place, Post believes that enlarging OPIC's financial support would help put the InterArab Fund in an excellent position to make a positive contribution to Jordan's business and financial community, and thereby contribute to spurring greater foreign and domestic investment in the Jordanian economy. Such a fund would find synergies with USAID-supported programs and with other investment funds being created in Jordan. A new \$50 million "Jordan Fund," for example, is financed by the Jordanian government and managed by the local Foursan Group with help from Deutschebank New York. Jordan Fund management told us that while they would look forward to working with a professionally managed InterArab Fund, and that both funds would be strengthened by the competition to find good projects. The Embassy would look forward to working with OPIC and a reinvigorated InterArab Fund to help make it another important piece of the U.S.-Jordan economic success story.

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